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C O N F I D E N T I A L CARACAS 000805

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SUBJECT: EXXONMOBIL MEETS WITH THE GOV

REF: CARACAS 163 (NOTAL)

Classified By: Economic Counselor Richard Sanders; for reasons 1.4 (b) and (d)

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SUMMARY  
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1. (C) ExxonMobil representatives met with Vice Minister of Energy and Petroleum Bernard Mommer on March 15 in what they termed a "cordial" meeting. This was the first meeting the company had won in its attempt to engage the GOV on its unilateral decision to increase the royalty levied on the four projects that upgrade the extra heavy oil of Venezuela's Orinoco heavy oil belt. ExxonMobil also received official notification in early March that the GOV had unilaterally raised a similar concessionary royalty rate on its La Ceiba project to 16.67 percent. ExxonMobil believes it will have a second meeting with the GOV the first week in April. A company manager stated his belief that ExxonMobil will have to think outside the box in order to identify a resolution that will allow the GOV to save face and claim victory in front of the other investors in similar projects. End Summary.

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EXXONMOBIL MEETS WITH VICE MINISTER  
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2. (C) ExxonMobil de Venezuela President Mark Ward met on March 15 with Energy and Petroleum Vice Minister Bernard Mommer. The purpose of the meeting was to discuss the unilateral decision taken by the GOV to increase the royalty on ExxonMobil's Cerro Negro project to 16.67 percent. (Note: ExxonMobil and other international oil companies embarked on what were then technically challenging multi-billion dollar investments in the 1990's. The projects received a 1 percent royalty rate for a nine year period. On October 10, President Chavez announced a GOV decision to increase the royalty to 16.67 percent. End Note.) Ward was accompanied by Caracas Government Affairs Manager Carlos Rodriguez who contacted econoff on March 16 with the report that Ward had characterized it as a "cordial" meeting. Mommer had, said Rodriguez, explained at length Venezuela's alleged right to make such a sovereign decision. He had urged ExxonMobil not to consider the arbitration route, and made a reference to the impact such a decision would have on ExxonMobil's other operations and opportunities in Venezuela.

3. (C) Rodriguez said Ward had underlined to Mommer that ExxonMobil has been an excellent business partner for the Chavez Government, noting that the company had been the first private sector company to ship a cargo out of Puerto La Cruz's Guaraquao terminal following the 2002-2003 oil strike, and had also signed the Preliminary Development Agreement for its proposed multi-billion dollar petrochemical project just two days before the August 2004 presidential referendum.

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AFTER MORE BAD NEWS  
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4. (C) Rodriguez informed econoff the week of March 7 that ExxonMobil had also received notice from the Ministry that the royalty on its La Ceiba project would be increased to 16.67 percent. The La Ceiba block is located in Trujillo state and was acquired by Mobil in the so-called "Exploration Round" in January 1996. The project is currently a joint venture with Petro-Canada. The partners drilled five wells in La Ceiba between 1997-2001 and, in order to aid their decision on whether they will move ahead on project development, performed a long-term production test on two wells in late 2004.

5. (C) The only exploration round project that has already declared commerciality is the Corocoro field, ConocoPhillips' discovery in the Gulf of Paria West block. In conjunction with President Chavez's February 11 meeting with

ConocoPhillips CEO Mulva, the company agreed to change the

royalty structure from a sliding royalty tied to the project's internal rate of return to a flat 16.67 percent royalty. With this agreement in hand, the Ministry moved quickly to mandate a similar change for La Ceiba. This decision will undoubtedly have an impact on ExxonMobil's planning with respect to any attempt to move ahead with the La Ceiba project. The two royalty issues, i.e., Cerro Negro and La Ceiba, will, said Rodriguez on March 16, be handled by the company as a package.

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NEXT STEPS  
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16. (C) According to Rodriguez, the two parties will meet again the first week in April. He added that it was obvious to him that the word "compensation" must be removed from ExxonMobil's lexicon to be replaced perhaps by "business opportunities." ExxonMobil will, he believes, have to "think outside the box" in order to identify a resolution that will allow the GOV to save face and claim victory in front of the other investors in similar projects.

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COMMENT  
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17. (C) In a February 28 meeting with the Ambassador to discuss the status of his attempts to meet with the GOV, Mark Ward said ExxonMobil was preparing to register its request for international arbitration as early as the first week of April. That target date will now slip. While ExxonMobil would undoubtedly prefer a negotiated settlement with the GOV, we do not believe the company will allow itself to be strung along at length. We also assume that the GOV would prefer to avoid potentially long-term litigation, but the designation of an appropriate "business opportunity" for ExxonMobil - perhaps preferential access to an off-shore gas block - might not be in line with President Chavez's recent preference for potential business deals with state oil companies from such partners as China, Russia, India, and Iran.  
Brownfield

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